

FISCAL NOTE

HB 2354 - SB 2326

March 13, 2007

SUMMARY OF BILL: Increases the excise tax on cigarettes from 20 cents to 60 cents per pack, effective July 1, 2007.

ESTIMATED FISCAL IMPACT:

Increase State Revenues - \$221,940,000 / General Fund
\$7,198,000 / Education Fund
\$41,000 / Department of Revenue
\$102,000 / Sinking Fund

(An amount equal to \$219,600,000 is included in the Governor's FY07-08 Budget Document)

Increase State Expenditures - \$200,000 One-Time
\$220,000 Recurring

Increase Local Govt. Revenues - \$4,062,000

Cigarette Tax Assumptions:

- Included in the Governor's FY07-08 Budget Document.
- According to the Department of Revenue (DOR), excise tax collections on cigarettes in FY05-06 were approximately \$115,462,000.
- Current excise tax rate on cigarettes is \$0.20 per pack.
- Estimated number of packs sold in FY05-06 was 577,310,000 ($\$115,462,000 \div \$0.20 = 577,310,000$ packs).
- Cigarette elasticity is estimated from a variable elasticity schedule depending upon the extent of any excise tax increase.
- Cigarette elasticity rate for proposed increase is estimated to be -0.279.
- Current state sales tax rate on cigarettes is 7.00%.
- Local option sales tax rate on cigarettes is estimated to average 2.25%.
- Current consumer price per pack is estimated to be \$3.19 per pack (excluding sales tax); \$3.49 per pack (including sales tax).

- Increasing the excise tax on cigarettes by \$0.40 per pack would also generate an additional \$0.04 per pack in state and local option sales tax revenue ($\$0.40 \times 9.25\% = \0.037).
- The total price increase to the consumer is estimated to be \$0.44 per pack ($\0.40 excise tax increase + $\$0.04$ incremental sales tax = $\$0.44$).
- Consumer price per pack after the proposed excise tax increase is estimated to be \$3.59 per pack (excluding sales tax); \$3.93 per pack (including sales tax).
- Increasing the excise tax on cigarettes would increase the price per pack to the consumer by an estimated 12.61% ($\$0.44 \div \$3.49 = 12.61\%$).
- Quantity demanded would decrease by an estimated 3.52% ($12.61\% \text{ price increase} \times -0.279 \text{ elasticity rate} = -3.52\%$).
- Quantity demanded in FY07-08 is estimated to be 556,988,700 packs ($577,310,000 \times \{100.00\% - 3.52\%\} = 556,988,688$).
- Total excise tax collections are estimated to be \$334,193,000 ($556,988,700 \text{ packs} \times \$0.60 \text{ excise tax} = \$334,193,220$) in FY07-08.
- Incremental excise tax collections are estimated to be \$223,632,000 ($\$334,193,000 - \$115,462,000 = \$218,731,000$) per year.
- 100% of the estimated \$218,731,000 in incremental excise tax collections would be apportioned exclusively to the General Fund.
- Sales tax collections will increase because sales tax is computed on the final retail sale.
- Retail sales before the proposed excise tax increase are estimated to be \$1,841,619,000 ($577,310,000 \text{ packs} \times \$3.19 \text{ old price (excluding sales tax)} = \$1,841,618,900$).
- Retail sales after the proposed excise tax increase are estimated to be \$1,999,589,000 ($556,988,700 \text{ packs} \times \$3.59 \text{ new price (excluding sales tax)} = \$1,999,589,433$).
- Incremental retail sales are estimated to be \$157,970,000 ($\$1,999,589,000 - \$1,841,619,000 = \$157,970,000$).
- Incremental state sales tax revenue is estimated to be \$11,058,000 ($\$157,970,000 \times 7.00\% \text{ state rate} = \$11,057,900$) per year.
- The \$11,058,000 in incremental state sales tax revenue would be apportioned as follows: \$3,209,000 to the General Fund, \$7,198,000 to education, \$508,000 to local governments, \$41,000 to the DOR, and \$102,000 to the Sinking Fund.
- The net recurring increase to state revenues resulting from incremental state sales tax collections is estimated to be \$10,550,000 ($\$11,058,000 - \$508,000 \text{ local share} = \$10,550,000$) per year.
- The total net recurring increase to state revenues resulting from the increased excise tax is estimated to be \$229,281,000 ($\$218,731,000 \text{ from additional excise tax} + \$10,550,000 \text{ from additional sales tax} = \$229,281,000$) per year.
- Incremental local option sales tax revenue is estimated to be \$3,554,000 ($\$157,970,000 \times 2.25\% \text{ local option rate} = \$3,554,325$).

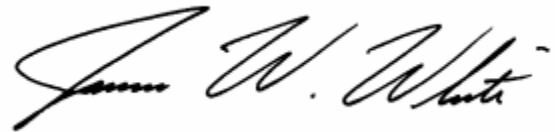
- The total net recurring increase to local government revenues resulting from the increased excise tax is estimated to be \$4,062,000 (\$3,554,000 in local option tax revenue + \$508,000 in state-shared sales tax revenue = \$4,062,000).

Other Assumptions

- Three additional Regulatory Officers in the DOR will be required to combat the illegal importation of cigarettes into Tennessee.
- Security upgrades will be required for cigarette tax stamps to combat illegal/counterfeit tax stamps.
- The recurring increase to state expenditures for the new positions and tax stamp enhancements is estimated to be \$220,000 per year.
- The one-time increase to state expenditures for computer and software enhancements and for costs associated with hiring the three Regulatory Officers is estimated to be \$200,000.

CERTIFICATION:

This is to duly certify that the information contained herein is true and correct to the best of my knowledge.

A handwritten signature in black ink, reading "James W. White". The signature is fluid and cursive, with the first name "James" and last name "White" clearly legible.

James W. White, Executive Director